



National Credit Union Administration

September 26, 2017

RE: Fidelity Bonds – Joint Coverage

NCUA has been asked if certain joint coverage provisions in fidelity bonds are permissible under the “individual policy” requirement of § 713.3(a) of NCUA’s regulations.¹

It is the opinion of NCUA’s Office of General Counsel (OGC) that the “individual policy” requirement of § 713.3(a) generally prohibits joint coverage under fidelity bonds, but does not prohibit a credit union from purchasing a fidelity bond that covers both the credit union and certain of its CUSO(s). This opinion is consistent with the Federal Credit Union Act (the Act) and NCUA’s previous approvals of various bond forms. This legal opinion rescinds and replaces previous legal opinions from this Office addressing the “individual policy” requirement of § 713.3(a) NCUA’s regulations.

Background

Section 713.4(b) requires NCUA to approve any bond form before a credit union may use it.² After the NCUA approves a bond form, it must also approve any changes or amendments to that form.³ Historically, NCUA’s process has been to focus on the changed portions of an approved bond form. This has been the case with joint coverage provisions, which, based on our research, have been included in approved bond forms prior to a 1999 regulatory change requiring individual coverage for every credit union (NCUA’s regulation is discussed in greater detail below). The following three types of joint coverage provisions have been included in various bond forms approved by NCUA:

1. **Nominee provision** – This provision states that a loss sustained by any “nominee” organized by the insured for the purpose of handling certain of its business transactions and composed exclusively of its employees shall be deemed to be loss sustained by the insured.
2. **Joint Insureds** – This provision explains how claims can be submitted if there is more than one insured under the policy and how losses are administered.
3. **Definition of Insured** – The definition of insured includes any subsidiary that is owned directly or indirectly by the insured in an amount greater than 50%.

¹ 12 C.F.R. § 713.3(a).

² *Id.* at 713.4(b).

³ *Id.*

NCUA Authority

The Act directs NCUA to require fidelity bond coverage for employees of federal credit unions who handle funds or collateral. The pertinent portion of the Act is quoted here, with bracketed numbers added for easier reference:

The Board is ... directed to require that every person appointed or elected by any Federal credit union to any position requiring the receipt, payment, or custody of money or other personal property owned by a Federal credit union or in its custody or control as collateral or otherwise, give bond [1] *in a corporate surety company holding a certificate of authority from the Secretary of Treasury* ... as an acceptable surety on Federal bonds. Any such bond or bonds [2] *shall be in a form approved by the Board* with a view to providing surety coverage to the Federal credit union with reference to [3] *loss by reason of acts of fraud or dishonesty* including forgery, theft, embezzlement, wrongful abstraction or misapplication [4] *on the part of the person, directly or through connivance with others*, and [5] *such other surety coverages as the Board may determine to be reasonably appropriate* or as elsewhere required by... [the Act]. Any such bond or bonds shall be [6] *in such an amount ... in relation to the assets of the Federal credit union as the Board may from time to time prescribe by regulation*[.] ... In lieu of individual bonds the Board may approve the use of a form of schedule or blanket bond which covers all of the officers and employees[.]⁴

The Act, in clauses [1] – [6], sets requirements for all fidelity bonds. Clauses [2] and [5] provide discretion for the Board to stipulate the form of the bond and to require additional "reasonably appropriate" coverage. Nothing in the Act addresses joint coverage.

Part 713 of NCUA's regulations implements the requirements of the Act and describes the fidelity bond and insurance coverage required for federal credit unions. This part is made applicable to federally insured, state-chartered credit unions by § 741.221 of NCUA's regulations.⁵ Section 713.3 requires that a bond, at a minimum, must be purchased in "an individual policy."⁶ NCUA added this section to Part 713 in a 1999 final rule in response to a commenter who pointed out that there had been instances of credit unions jointly purchasing fidelity bonds.⁷ The commenter was concerned that a loss caused by one or two of the joint policy holders could reduce the amount of available coverage below the required minimum amount for the other policy holders. In addressing this comment, the Board clarified § 713.3 to provide that a credit union must purchase its own individual policy.⁸ The regulation did not, however, define "individual policy."

⁴ 12 U.S.C. § 1766(h) (emphasis added).

⁵ 12 C.F.R. § 741.221.

⁶ *Id.* at § 713.3.

⁷ 64 Fed. Reg. 28718, 28719 (May 27, 1999).

⁸ *Id.* at 28719.

Since inclusion of this provision in NCUA's regulations, this Office has issued two public legal opinions interpreting the meaning of "individual policy" and opining on the type of coverage that is prohibited under § 713.3(a). A 2014 legal opinion states that a federally insured credit union may not include one or more of its CUSOs or other parties as additional insureds under its fidelity bond.⁹ In a 2004 legal opinion, this Office opined that a CUSO that provides management services for multiple credit unions could not purchase a single fidelity bond with each credit union named as an insured.¹⁰ In both letters, this Office explained that the purpose of the individual policy requirement is to avoid diluting or conflicting with the individual credit union's coverage.

Opinion

As noted above, this Office is changing its opinion of the permissibility of certain joint coverage provisions to clarify the permissibility of the prior bond forms approved by NCUA. As the individual policy requirement is neither a statutory requirement nor defined in the current regulation, but rather has been defined by OGC legal opinions, the agency may change its legal interpretation by revising its legal opinions. Courts generally give agencies discretion in interpreting their own regulations and have held that an agency is free to amend its interpretation of its regulations at any time, provided the agency acknowledges the action and provides an explanation to the public.¹¹ This opinion acknowledges the agency's change in position and explains that change.

In the past, NCUA's review did not focus on the joint coverage provisions that had been included in approved bond forms before the 1999 regulatory change. It is clear from our recent review of this issue, however, that the previous two legal opinions similarly did not address the issue of joint coverage in bond forms that NCUA had approved in the past. This has resulted in an inconsistency between NCUA's approvals and this Office's legal opinions.

It is the opinion of this Office that the "individual policy" requirement does not prohibit a credit union from having a fidelity bond that also covers its CUSO(s), provided the credit union owns at least 50% of the CUSO or the CUSO otherwise meets the definition of a "nominee," as defined above. The "individual policy" requirement does, however, continue to prohibit joint coverage of entities not majority owned by the insured credit union, such as other credit unions or non-majority-owned CUSOs. This is in alignment with the purpose of the rule and NCUA's prior practices. This opinion does not change the minimum required dollar amount of coverage under § 713.5 or the ability of the Board to require additional coverage under § 713.7.¹²

NCUA recently published a proposed regulatory reform agenda, which includes a recommendation from NCUA's Regulatory Reform Task Force to explore revisions to Part 713 in the first 24 months of the agenda.¹³

⁹ OGC Legal Op. 14-1013 (Mar. 21, 2014).

¹⁰ OGC Legal Op. 04-0744 (Sep. 21, 2004).

¹¹ F.C.C. v. Fox Television Stations, Inc. 556 U.S. 502, 515 (2009).

¹² 12 C.F.R. §§ 713.5 and 7.

¹³ 82 Fed. Reg. 39702, 39706 (Aug. 21, 2017).

September 26, 2017

Page 4

If you have any further questions, please contact Senior Staff Attorney Justin M. Anderson.

Sincerely,

A handwritten signature in blue ink, appearing to read "Michael J. McKenna", with a long horizontal flourish extending to the right.

Michael J. McKenna
General Counsel

GC/ JMA
SSIC 3000
17-0959